

West Suffolk Investment Framework

1. Background

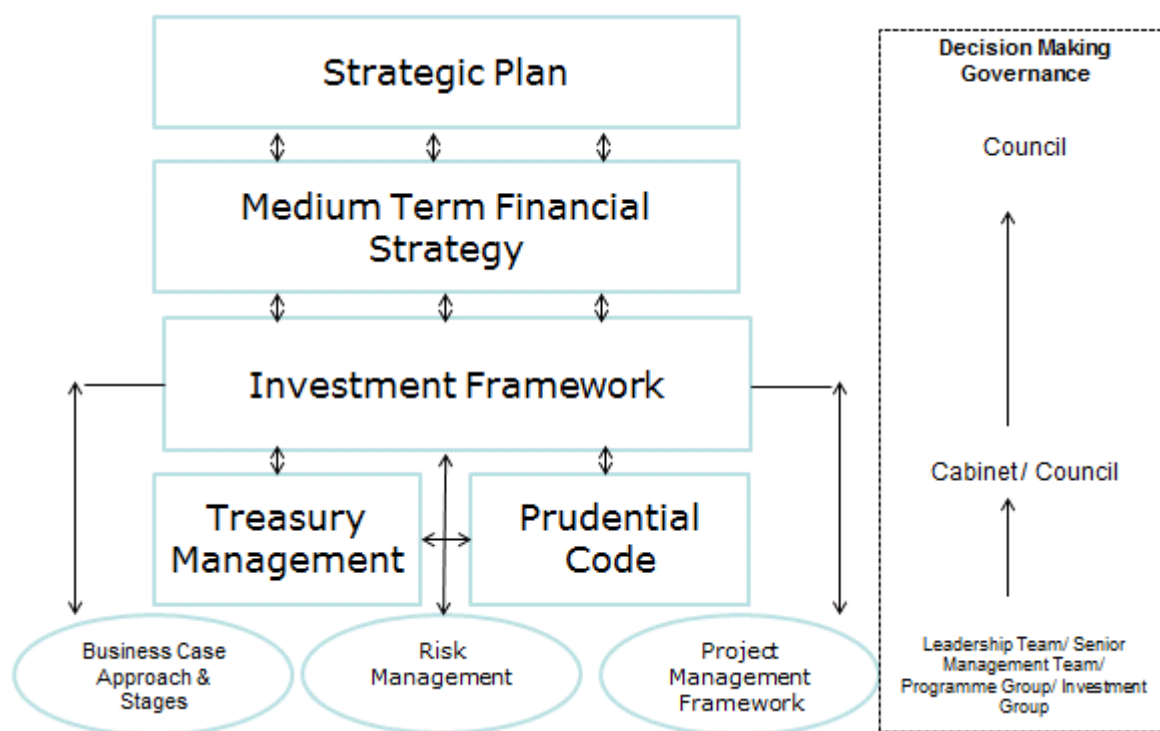
- 1.1 The West Suffolk Medium Term Financial Strategy (MTFS) sets out the approach that Forest Heath District Council and St Edmundsbury Borough Council will take to the sound management of their finances over the medium term to ensure the Councils can meet our shared priorities set out in the West Suffolk Strategic Plan (SP), and to continue to carry out the day-to-day responsibilities within a financially constrained environment.
- 1.2 The MTFS sets out West Suffolk's response to the financial challenges and opportunities both councils have in common across six key themes; including 'behaving more commercially', 'being an investing authority' and 'taking advantage of new forms of local government finance'. The inclusion of these themes within the MTFS, along with key investment projects within the Strategic Plan demonstrates both councils' commitment to continue with our long tradition of investing in our communities. This commitment to investment supports the delivery of our shared strategic priorities, in particular to aid economic growth across West Suffolk.

2. Introduction

- 2.1 With the emphasis on 'investing' in key strategic projects to support the delivery of the shared priorities, it is important that both councils set out their approach to considering each project on its own merits alongside a set of desired collective 'investing' programme outcomes. This is particularly important when set against the backdrop of continued financial challenges for local government associated with medium to long term funding uncertainties.
- 2.2 These desired collective 'investing' programme outcomes will act as an 'investment framework' to support staff and members throughout the initial development stages to the decision making stages of our key strategic projects, particularly those that require the Councils to invest.
- 2.3 Such an 'investment framework' would also support the Councils' compliance with 'The Prudential Code for Capital Finance in Local Authorities (the Code)'. Key objectives of the Code are to ensure, within a clear framework, that local authorities' capital investment plans are affordable, prudent and sustainable; that treasury management decisions are taken in accordance with good professional practice; and that local strategic planning, asset management planning and proper option appraisal are supported.

3. A proposed West Suffolk Investment Framework

- 3.1 The diagram below sets out where this 'investment framework' sits within the wider strategic priorities and decision making process.



- 3.2 It is important that each key strategic project is considered on its own individual merits, detailed in each business case, as part of the Councils' democratic decision making process. However, it is envisaged that each investment decision is also to be considered against a set of proposed collective 'investing' programme outcomes.
- a. Each project will be subject to a highly competent professional business case.
 - b. Each project will need to demonstrate that it positively contributes towards the delivery and desired outcomes set out in the West Suffolk strategic priorities, unless investment is required to maintain our statutory obligations.
 - c. Each project will be assessed for the opportunity for innovative delivery and/or financing solution(s), exploring where appropriate investments away from the traditional local government funding models.
 - d. Each project and potential partner will be considered against the general ethos and values of local government and the wider public sector.
 - e. Each investment project will be assessed on the basis of borrowing and its cost, assessing each project on a level playing field regardless of its timings within the MTFs or the funding model using a target 10% internal rate of return (IRR) (linked to cash flows) will be set in order to cover the cost of borrowing.
 - f. Achievement against the IRR is not mandatory where the business case can demonstrate that the project outcomes are focused on the non-financial benefits for the residents of West Suffolk and/or for the wider public sector (i.e. where it meets the councils' wider devolution plans).
 - g. Projects will be considered as West Suffolk projects unless there are compelling financial or demographic reasons not to do so. Each West Suffolk project business case will detail, ready for the democratic process, the individual Council's investment, return, risk and governance considerations/implications.
 - h. Each project will be assigned an overall investment risk, based on an assessment of the individual business cases including risk and likelihood of

returns, (high, medium or low) in order to manage the councils' overall investment portfolio and exposure.

- i. Each project will be assessed against the councils' wider capital programme commitments/aspirations and asset management plans to ensure that the overall capital programme is affordable, prudent and sustainable.
- j. Each project will follow the councils' project management framework both through its development and implementation and will include a project close-out phase so that lessons learnt can be captured for future projects.
- k. Each project that requires the formation of a new governance structure or new legal entity will be considered against a number of key considerations, with each project being considered on its own merits:
 - Project outcomes
 - Legal powers
 - Procurement
 - Council ownership and liabilities
 - Financial returns
 - Taxation
 - Risk
 - Governance structure and skill requirements
 - Exit strategy

4. West Suffolk projects vs FHDC and SEBC projects

- 4.1 In line with the collective 'investing' programme outcomes above, new projects will be considered as West Suffolk projects unless there are compelling financial or demographic reasons not to do so.
- 4.2 This may involve joint shareholding interests or joint investment and return opportunities associated with a sharing of the project risks and rewards. Therefore each West Suffolk project business case will detail, ready for the democratic process, the individual Council's investment, return, risk and governance considerations/implications.
- 4.3 Some projects may involve other public and/or private sector partners alongside the West Suffolk authorities. In these projects West Suffolk will strive to achieve the appropriate shareholding, influence and outcomes for West Suffolk, including those times where the West Suffolk authorities may only hold a minority shareholding and/or interest.

5. West Suffolk Business Case approach and stages

- 5.1 In support of the West Suffolk SP and MTFs, it is vital that capital spending decisions are taken on the basis of highly competent professionally developed business cases. Business cases for each strategic project will follow a five stage approach. Appendix 1 describes each of the stages in the development of a well-prepared business case which supports evidence-based decisions. This approach also provides a clear audit trail for purposes of public accountability.

- 5.2 The business case, both as a product and a process, provides decision makers, stakeholders and the public with a management tool for evidence-based and transparent decision making and a framework for the delivery, management and performance monitoring of the resultant scheme.
- 5.3 The business case for each key strategic project must evidence the following evidence.:
- i. **Strategic case** - The case for change, delivery of the Councils' Strategic Priorities, the project's holistic fit with other parts of the organisation and public sector.
 - ii. **Economic case** - The project represent best public value.
 - iii. **Commercial case** - The project is appropriate to its market place, can be accomplished and is commercially viable.
 - iv. **Financial case** - The project is affordable and sustainable.
 - v. **Management case** - The requirements from all the project parties are quantifiable and achievable.
- 5.4 Business cases should be developed over time. Development is an iterative process and at each key stage further detail is added to each of the five dimensions above. The level of detail and the completeness of each of the five dimensions of the case are built up at different rates during the process.

6. Feasibility funding

- 6.1 A number of our key strategic projects have the potential to commit significant capital sums, as well as officer and member resources. It is also the case that at the early stages of a project, the desired outcome(s) may be achieved through a number of different options which need to be investigated further.
- 6.2 Alternatively, work may be needed to ascertain whether a project is deliverable and represents value for money for tax payers before large capital sums are committed and potentially placed at risk. It is important that, where appropriate, feasibility funding is made available as it often unlocks the full capital investment potential and provides the necessary progress to stage three (approval) of the business case development.
- 6.3 For all these reasons, feasibility funding is often requested at the early stages of a project to support the development of options and the identification of a preferred way forward for member scrutiny and approval.
- 6.4 Stages one (concept) and two (deliverability and design) of our West Suffolk business case approach covers the feasibility stages of a project. Feasibility funding is therefore likely to be requested to support these two stages along with the development of the business case to stage three (approval), where the capital investment is likely to then be requested.
- 6.5 Feasibility funding may be sought in stages, both reflecting the importance of member support at each stage of a business cases development and to minimise the overall financial exposure (both externally and internally committed) for the councils.

- 6.6 Feasibility funding can cover a number of different aspects depending on scale, complexity and nature of the project. Typical feasibility costs can include the following.
- i. Project management support to co-ordinate and manage all the specialist skills engaging in the development of the business case and for management and member briefings. Although likely to be allocated at the outset, this resource/skill is often mobilised for the full five business case stages.
 - ii. Legal considerations and structures, including the power to enter into the proposed project, governance considerations and procurement considerations.
 - iii. Financial considerations including financing options, revenue and capital impacts, tax implications and governance considerations.
 - iv. Financial modelling including sensitivity analysis across the various options and then more detailed analysis on the preferred way forward.
 - v. Risk considerations covering business case option(s), legal, financial, governance, mitigation strategies and exit strategies.
 - vi. Commercial considerations including market and consumer analysis, links into financial modelling, risks, best value and valuation services.
 - vii. Planning services where planning considerations are required.
 - viii. Communications including public consultation/engagement on options.
 - ix. Technical/professional services where the project involves specific technical/professional analysis and/or commentary.
- 6.7 It is likely that certain key projects, due to their nature, complexity, scale or overall capacity will require the appointment of external skills and/or resource. This is particularly true where the Councils are exploring opportunities that are not within the skill set of officers as they are new service developments such as financial modelling work for housing investment options which include the development and construction of housing for mixed tenure.
- 6.8 External services may also need to be appointed where there are a number of partners involved, when it is considered appropriate to appoint an independent resources/skill such as a property valuer.
- 6.9 Taking a sample of investments either currently being considered or already implemented, a possible benchmark for such feasibility costs is up to 5% of total capital investment value, again this would depend on the nature, complexity and scale of the project. A large proportion of these costs are able to be capitalised (the Council would be required to assess whether the costs meet the definition of capital, which if the scheme is expected to proceed it is likely they would). However, some of the early feasibility costs covering exploration of a number of options may not be able to be capitalised (under current accounting rules) as they are not directly linked to bringing the project/asset into use under the final option. Also if a project does not proceed beyond phase one or two of the business case development, then feasibility funding would be regarded as abortive costs and would be deemed to be revenue (under current accounting standards).

- 6.10 It is for these reasons that feasibility funding is normally proposed to be covered initially by a revenue budget/reserve at the outset, enabling us to manage transparently our revenue exposure to these capital investment opportunities in the event of the projects not proceeding. Once the project proceeds beyond phase three of the business case development then there is the opportunity for us to capitalise some of those costs from phase one and two giving us a choice then over the funding basis if we wish to change this from revenue to capital for wider financial management/planning reasons.
- 6.11 Where a project involves more than one partner it may be that a lead authority is assigned up front incurring all feasibility costs and then recharging on an agreement basis or it may be that each partner commissions different elements of the feasibility work with an open book approach to recharging once the feasibility is concluded, again on up front agreed split.

7. The Financial Case and Project Financing

- 7.1 Depleting capital and revenue reserves and increased pressure on external funding mean that both councils may want to consider investing away from the traditional funding models such as using its own reserves. Instead focus is now on the use of:
- i. making loans, securing the return of the council's funds;
 - ii. joint ventures, sharing the investment required; or
 - iii. borrowing, introducing new funds into both councils.
- 7.2 The financing of the chosen funding model itself is a challenge for both councils with limited reserve balances available in the medium to longer term. In order to generate new cash into the authorities and to enable a position of becoming 'investing authorities' means that borrowing, in order to create new cash, is something that both councils are open-minded about.
- 7.3 The choice of funding models for each investment opportunity/project will be based on their individual merits, financial return/costs including the comparison to the agreed target internal rate of return and overall risk exposure, considered as part of each business case. Any decision to invest or borrow would be subject to full scrutiny by councillors, through the usual democratic process.
- 7.4 There are ample precedents which demonstrate that prudential borrowing has become a valuable tool for local government to achieve its strategic objectives. The use of unsupported borrowing (no security to a particular council asset) is both flexible and relatively straightforward.
- 7.5 With this in mind and as borrowing is likely over the medium to long term for both authorities, it is considered prudent to assess each investment opportunity/project on the basis of borrowing and its cost, assessing each

project on a level playing field regardless of their timings within the MTFS or the funding model used.

- 7.6 There are two annual revenue costs associated with borrowing:
- a. servicing the debt – the interest payable on the loan; and
 - b. repayment of the loan/capital by the Councils – effectively through a minimum revenue provision (MRP).
- 7.7 At the time of writing this framework, these costs would be in the region of 4.5% interest (based on a Public Works Loan Board –PWLB, rate over 25 years) and 4% MRP, and therefore in order to assess each project on a level playing field a target 10% internal rate of return (IRR) will be set in order to cover the cost of borrowing. It may be that when a granting of a loan is considered by the Councils and MRP is not deemed to be applicable as it can be demonstrated that the repayment cost provision provided for by the MRP element is not required because the loan has a robust repayment schedule (a security), so a lower IRR could apply.
- 7.8 Naturally a change in interest rate or MRP rate would change the target rate of IRR.

8. Treasury Management Strategy and Practices

- 8.1 Both Councils' capital investment plans and day-to-day revenue budget plans inform the development of our Treasury Management and Investment Strategies, which are agreed annually as part of the budget setting process by each Council.
- 8.2 The Councils define our treasury management activities as:
"The management of the organisation's cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and pursuit of the optimum performance consistent with those risks".
- 8.3 The assessment of each strategic investment project on the basis of borrowing and its cost, on a level playing field, regardless of its timings within the MTFS or the funding model used, enables the Councils to assess our capital investment plans for affordability, prudence and sustainability. This assessment must take place at the financial case and project financing stage to enable Members to understand the longevity of the impact of their capital investment decisions on the Councils' revenue budgets.
- 8.4 The cost of borrowing determined in each business case will be placed within the Councils' revenue budgets to protect the revenue budget as a result of the capital investment decision made. At the In reality as the Councils still holds both:
- usable capital receipts - once these run out this is when MRP is required; and

- healthy cash flow balances - when these run out this is when external interest becomes payable as a loan has been taken out by the Councils to support cash flow requirements.

The actual point of borrowing and therefore the costs associated won't necessarily be straight away or for the amounts detailed within each of the aggregated business cases. That is because it's not prudent for the Councils to borrow until the cash in the bank is running out so the actual borrowing process is a matter for the Treasury Management team to manage in line with the agreed Treasury Management and Investment Strategies.

- 8.5 Annually as part of the wider budget setting process, for scrutiny by members, the Councils' Chief Financial Officer will look to determine the Councils' actual borrowing requirements and therefore expected borrowing costs based on the current and future cash flow requirements (i.e. treasury management activities). Any difference between the aggregation of each business case cost of borrowing and the actual borrowing costs (MRP and external interest) will effectively be a treasury management saving for the Councils over and above those savings determined in the business case. These treasury management savings effectively come about from what is referred to as internal borrowing by the Councils rather than external borrowing.
- 8.6 It would be correct to assume therefore a shift in focus for the Councils' Treasury Management and Investment Strategies over the coming years from the current cash investment emphasis to a much greater focus on cash flow management and modelling, and to minimise our actual short and long term borrowing requirements from sound treasury management planning and decisions.

9. Project/Programme Management

- 9.1 Programme and Project Management is about 'doing things right' and is the process of delivering the projects and overall programme and providing assurance to Members on the delivery of our projects objectives and strategic outcomes. This includes a strong emphasis on planning project activities; managing key relationships; setting priorities; evaluating implementation and reporting on the delivery of projects.
- 9.2 Our new approach to programme and project management has been developed to be as agile and responsive as possible. We are providing support and guidance for our managers to take on project management responsibility and develop the skills needed to deliver effective projects with successful outcomes.
- 9.3 Our project management approach has been designed to provide a structured environment for projects to flourish, while being flexible enough to respond to the needs of an array of projects across the organisation. This approach relies on a fundamental grasp of the foundations of good project management and being able to lead projects successfully rather than being focused on one methodology or software package.
- 9.4 The officer Programme Group, supported by the Councils' Programme Manager, ensures that senior managers work together to ensure the effective delivery of Councils' projects. As part of this assurance framework the Group review and

monitor all aspects of project development, delivery and management of projects across the West Suffolk Councils; ensuring there is oversight and co-ordination of core projects, with the purpose of improving overall development and delivery of projects as well as collective responsibility.

- 9.5 By adopting this approach it is possible to ensure that the key risks and issues that will impact on a project are assessed and that appropriate mitigation is in place. Further it enables any relevant policy considerations to be taken into account throughout the course of any project.
- 9.6 From time to time it may be that individual projects, due to their nature, complexity, scale or overall capacity; require external project management skills and/or resource. Where external appointments take place the project management responsibilities are often also linked to any gaps identified in the professional/specialist skills/capacity category such as a property specialist leading as a project manager for a complex property project. External project managers may also need to be appointed where there are a number of partners involved, when it is considered appropriate to appoint an independent project management lead.
- 9.7 External project management costs are often identified early on in the feasibility funding stage(s) and these skills/resources are often mobilised for the full five business case stages.

10. Risk Management approach

- 10.1 Our new, positive approach to risk is based on context, proportionality, judgement and evidence-based decision making that considers each capital investment project on case by case basis and is documented at all stages. We aim to be joined-up in our decisions, and draw on one another's skills and experience to take responsibility for sound and reasonable decisions about the use of public funds, avoiding a blame culture when things don't necessarily go to plan.
- 10.2 Our approach, detailed in our 'risk management approach' document, is based on seven core principles:.
- i. a positive approach;
 - ii. contextual decision making;
 - iii. informed risk-taking;
 - iv. proportionality;
 - v. decision risks vs delivery risks;
 - vi. a documented approach; and
 - vii. continuous improvement.
- 10.3 Our approach to risk is just that, it's our approach. It isn't designed to have all the answers up front or to represent our risk appetite. It commits staff and members to evidence-based decision making that is considered on a case by case basis, taking into account the seven principles outlined above.

11. Business Case Governance – decision making

- 11.1 Business cases are developed following a number of governance parameters including those discussed above, i.e. around project and risk management. They are also delivered following the constitutional governance arrangements and delegations. Decisions falling outside of the key decisions definition for Cabinet will be the subject of a Council report. This is likely to be the case for many of our key strategic projects, especially where financial sums are involved above Cabinets' collective limits.

Business case development – five stages

Feasibility - Concept stage

- The purpose of this stage is to confirm the strategic context of the proposal and to make a robust case for change, providing stakeholders and customers with an early indication of the “preferred way forward” (not the preferred option). SWOT (strength, weaknesses, opportunities and threats) analysis on a wide range of available options is undertaken at this stage, together where possible with an early analysis of the shortlist which may, if available, be based on indicative costs and benefits.
- At this stage it is not possible to provide the detailed economic analysis, commercial, financial and management arrangements, hence these aspects are relatively under-developed at this stage.

Feasibility - Deliverability and design stage

- The purpose of this stage is to revisit earlier assumptions and analysis in order to identify a “preferred option” which demonstrably optimises value for money. It also sets out the likely deal; demonstrates its affordability; and details the supporting procurement strategy, together with management arrangements for the successful delivery of the proposal.

Approval stage

- The purpose of this stage is developing the full business case including the economic, commercial, financial and management cases and arrangements, to gain political approval for the project.

Delivery/Implementation stage

- This is the procurement and delivery phase for the spending proposal, following detailed negotiations with potential service providers/suppliers prior to the formal signing of contracts and the procurement of goods and services.
- The business case should be used during the delivery/implementation stage as a reference point for monitoring implementation and for logging any material changes that are required on the part of the procuring authority or the service supplier in respect of services and products.

Close out stage

- The business case and its supporting products should be used as the starting point for post-implementation evaluation, both in terms of how well the project was delivered (project evaluation review) and whether it has delivered its projected benefits as planned (post implementation review).